

1 UNITED STATES BANKRUPTCY COURT

2 SOUTHERN DISTRICT OF NEW YORK

3 Case No. 18-23538-rdd

4 Adv. Case No. 19-08700-rdd

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6 In the Matter of:

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8 SEARS HOLDINGS CORPORATION,

9

10 Debtor.

11 - - - - - x

12 VIR VENTURES, INC., et al.,

13 Plaintiffs,

14 v.

15 SEARS HOLDINGS CORPORATION,

16 Defendants.

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1 United States Bankruptcy Court
2 300 Quarropas Street, Room 248
3 White Plains, NY 10601

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5 March 25, 2020

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21 B E F O R E :
22 HON ROBERT D. DRAIN
23 U.S. BANKRUPTCY JUDGE
24

25 ECRO: UNKNOWN

1 HEARING re Notice of Agenda of Matters Scheduled for
2 Telephonic Hearing on March 25, 2020 at 10:00 a.m.

3
4 Adversary proceeding: 19-08700-rdd Vir Ventures, Inc. et al
5 v. Sears Holdings Corporation

6 Motion to Dismiss Adversary Proceeding / Debtors (I) Motion
7 to Dismiss the Adversary Complaint and (II) Reply to
8 Plaintiffs Opposition to Debtors Second Omnibus Claims
9 Objection (related document(s))1)

10
11 Adversary proceeding: 19-08700-rdd Vir Ventures, Inc. et al
12 v. Sears Holdings Corporation

13 Declaration of Jennifer Brooks Crozier, Esq. in Support of
14 Motion of Sears Holdings Corporation to Dismiss Adversary
15 Proceeding [ECF No. 13]

16
17 Adversary proceeding: 19-08700-rdd Vir Ventures, Inc. et al
18 v. Sears Holdings Corporation

19 Motion to Adjourn Adversary Proceeding or, in the
20 Alternative, for an Extension of Time to Answer or Otherwise
21 Respond to Plaintiffs' Adversary Complaint [ECF No. 5]

1 Adversary proceeding: 19-08700-rdd Vir Ventures, Inc. et al
2 v. Sears Holdings Corporation
3 Joint Response of VIR Ventures, Inc. and AMI Ventures, Inc.
4 in Opposition to Debtors Motion to Adjourn Adversary
5 Proceeding, or in the Alternative, for an Extension of
6 Time to Answer or Otherwise Response to Plaintiffs Adversary
7 Complaint [ECF No. 6]
8
9 PLAINTIFFS RESPONSE IN OPPOSITION TO DEBTORS MOTION TO
10 DISMISS THE ADVERSARY COMPLAINT (ECF 7457)
11
12 Debtors' Sixth Omnibus Objection to Proofs of Claim
13 (Satisfied Claims) [ECF No. 5075]
14
15 Motion for Extension of Time to File Memorandum of Law in
16 Compliance with Court Order [ECF No. 7448]
17
18 Notice of Sale: Notice of De Minimis Asset Sale for
19 Membership Interest in Clayton Street Associates, LLC
20 (related document(s) 856) filed by Jacqueline Marcus on
21 behalf of Sears Holdings Corporation (ECF 7335)
22
23 Objection of Broe Real Estate Group to the Debtors Proposed
24 De Minimis Asset Sale of Their Membership Interest in
25 Clayton Street Associates, LLC (related document(s) 7335)

1 Motion Addendum of Julie Independence Tomchak for Original
2 Motion (related to ECF #4209) (ECF 5483)

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4 Debtors' Objection (ECF 7475)

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25 Transcribed by: Sonya Ledanski Hyde

1 A P P E A R A N C E S :

2 WEIL, GOTSHAL & MANGES LLP

3 Attorneys for the Debtor

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6

7 BY: JENNIFER CROZIER

8 GARRETT FAIL

9 JACQUELINE MARCUS

10 PHILIP DIDONATO

11 JULIE TOMCHAK

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18 BY: JOHN BECK

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20 BERNSTEIN-BURKLEY, P.C.

21 Attorneys for the Plaintiffs

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25 BY: SALENE KRAEMER

1 ALSO PRESENT TELEPHONICALLY:

2

3 CHRIS STAUBLE

4 ARLENE R. ALVES

5 LAUREN BAILO

6 SARA BRAUNER

7 ALIX BROZMAN

8 BENJAMIN BUTTERFIELD

9 PATRICK J. HOLOHAN

10 HOO RI KIM

11 PAUL LABOV

12 CATHERINE LOTIEMPIO

13 MARILYN MACRON

14 HOWARD P. MAGALIFF

15 SHIRIN MAHKAMOVA

16 JENNIFER MARINES

17 ERIKA MORABITO

18 NERVILLE N. REID

19 LEE J. ROHN

20 SUNNY SINGH

21 ALEXANDER R. TIKIN

22 DAVID H. WANDER

23 MAGDALENA ZALEWSKI

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1 P R O C E E D I N G S

2 THE COURT: Okay, good morning. This is Judge
3 Drain in In re Sears Holdings Corp., et al. There's no one
4 in the courtroom except the person who's operating the
5 recording for transcription purposes. I know I have a lot
6 of people on the phone. I'll ask you to identify yourself
7 only when you're speaking and then you can not only state
8 who you are, but who you're representing.

9 So I have the amended agenda for today and I'm
10 happy to go down in the order of that agenda unless someone
11 wants to proceed in another way.

12 MS. CROZIER: Good morning, Your Honor. It's
13 Jennifer Crozier of Weil, Gotshal, and Manges for the
14 Debtors. The first item on the amended agenda, as you see,
15 is the Debtors' motion (audio cuts out) plaintiffs VIR
16 Ventures and AMI Ventures, the remaining counts of their
17 adversary complaints and given the circumstances, Your
18 Honor, I intend to be brief (audio cuts out) answer any
19 questions concerning the Debtors (audio cuts out).

20 THE COURT: Okay, well, this motion may take a
21 while, so notwithstanding what I just said, it's probably
22 better to go to the uncontested matters and the rest of the
23 agenda first and then we can come back to the VIR matter.

24 MS. CROZIER: Sure, that's perfectly fine with the
25 Debtors, Your Honor, and so I will hand it over to

1 (indiscernible) to address Item No. 2.

2 THE COURT: Okay.

3 MR. FAIL: Thank you. Thank you, Your Honor.

4 Garrett Fail, Weil, Gotshal, and Manges for the Debtors.

5 The first uncontested item is No. 2 on the agenda. It's the
6 Debtors' sixth omnibus objection to claims. The Debtors
7 objected to a number of claims on the basis that the claims
8 had been satisfied in full. The Debtors carried a number of
9 the claims from time to time as we continued to work with
10 the creditors that were subject to it. Today, we are going
11 forward on an uncontested basis with respect to three claims
12 filed by Salesforce.com.

13 We've received confirmation from Salesforce.com
14 they have no objection or no opposition to the objection,
15 and so we're just proceeding to submit a supplemental order
16 with respect to these claims.

17 THE COURT: Okay. That's fine, based on that
18 representation and there being no objection by Salesforce.
19 I will grant the objection as to those three claims. You
20 can email that order --

21 MR. FAIL: Thank you very much, Your Honor. Thank
22 you very much, Your Honor, and on behalf of the Debtors,
23 thank you again for accommodating our -- the hearing agenda
24 on the calendar under the circumstances.

25 THE COURT: That's fine. Okay.

1 MR. FAIL: The next item is the motion of Santa
2 Rose Mall and I believe counsel should be the line.

3 THE COURT: Do I have counsel for Santa Rosa on
4 the phone? All right. Well, I actually thought I had
5 granted this in an email response to counsel. The Debtors
6 have no objection to this request for an extension of time,
7 correct?

8 MS. MARCUS: Your Honor --

9 MR. FAIL: That's correct, Your Honor. Garrett
10 Fail. Go ahead.

11 MS. MARCUS: That's fine.

12 THE COURT: Okay, so I will grant this request.
13 I(actually don't think I need an order to do this, but if
14 counsel for Santa Rosa thinks I do, then they can email it
15 to chambers, but I grant the request which is on consent to
16 extend the deadline to submit its memorandum of law to the
17 27th of this month from the 13th.

18 MS. MARCUS: Your Honor, Jacqueline Marcus, Weil,
19 Gotshal, and Manges, on behalf of the Debtors. The next
20 item, No. 4 on the uncontested list is the notice of de
21 minimis asset sale for membership interest in Clayton Street
22 Associates, LLC. As indicated on the objection -- on the
23 agenda, excuse me, Your Honor, Broe Real Estate Group filed
24 an objection to the Debtors' proposed transaction that was
25 at ECF No. 4730, and by way of background, on February 24th,

1 the Debtors filed the notice of de minimis asset sale. At
2 the time, the Debtors proposed to sell their membership
3 interest in Clayton Street Associates, LLC, to NP, Inc.,
4 Nichols, for \$37,500 plus a 20 percent profit participation.

5 Clayton's plan was to exercise a right of first
6 refusal to acquire a valuable parking lot in Denver,
7 Colorado. After the sale notice was filed, the Debtors were
8 contacted by Broe Real Estate Group which indicated that it
9 was prepared to bid substantially more for the membership
10 interest. Broe filed its objection to the proposed
11 transaction along with a revised form of membership purchase
12 agreement that it was prepared to enter into.

13 The Broe officer provided a cash purchase price of
14 \$1,125,000 and Broe requested, as part of its offer that the
15 Debtors reimburse Broe's expenses of not less than \$50,000
16 if it were not the successful bidder for the membership
17 interest. Under the operating agreement for Clayton Street
18 associates, the other member of the company has the right to
19 match any proposed offer for the sale of a member's
20 interest. Accordingly, the Debtors provided Nichols with
21 notice of the Broe offer and requested that they either
22 match the offer or consent to the transfer of the membership
23 interest to Broe.

24 Nichols elected to match Broe's offer and the
25 Debtors and Nichols have entered into a revised membership

1 interest purchase agreement that provides for a purchase
2 price of \$1,125,000 conditioned upon the closing of the sale
3 of the parking lot to Clayton. The Debtors subsequently
4 requested that Broe withdraw its objection and Broe
5 requested that the Debtors agree to stay the expense
6 reimbursement.

7 After discussions with attorneys for the Creditors
8 Committee, and in view of substantial increase in the
9 purchase price precipitated by the Broe offer, the Debtors
10 have agreed, subject to the approval of the Court, to grant
11 Broe an allowed administrative claim in the amount of
12 \$50,000 which would be treated as a tier two, non-opt-out
13 claim under the administrative expense claims program.

14 The terms of the agreement with Broe are set forth
15 in the stipulation agreement that was filed with the Court
16 at ECF No. 7505 and a copy of the stipulation was provided
17 to chambers yesterday. As indicated, the key terms of the
18 stipulations are, upon Court approval, Broe's objection
19 shall be deemed withdrawn and the Debtors will be authorized
20 to complete the sale to Nichols in accordance with the
21 revised membership purchase agreement and Broe shall have an
22 allowed non-opt-out settled administrative claim pursuant to
23 the administrative expense claims consent program in the
24 amount of \$50,000 which shall be subject to the 80 percent
25 recovery (indiscernible).

1 Additionally, the Debtors and Broe release each
2 other from any claims related in any way to the membership
3 interest and sale notice or the objection. Your Honor, from
4 the Debtors' point of view, the sequence of events
5 represents an excellent outcome, and accordingly, the
6 Debtors request that the Court approve the stipulation. I'm
7 happy to answer any questions that you might have.

8 THE COURT: Okay. Is anyone from Broe Real Estate
9 on the phone? I don't think so.

10 MR. BECK: Yes, Your Honor.

11 THE COURT: Oh, you are. Okay.

12 MR. BECK: Yes, Your Honor. This is Beck -- John
13 Beck of Hogan Lovells.

14 THE COURT: Okay. Is there any agreement or
15 understanding between the actual buyer here or proposed
16 actual buyer and Broe with respect to the subsequent
17 transfer of the property?

18 MR. BECK: No, Your Honor, there --

19 THE COURT: Okay. All right. I will grant the
20 motion as revised and also enter -- approve the Debtors'
21 entry into the stipulation with Broe. That is on the
22 condition, though, that there be no agreement or
23 understanding as between Broe or anyone acting on its
24 behalf, and the actual buyer here that -- with respect to
25 any subsequent transfer of the property from the buyer from

1 the Debtor to Broe or anyone connecting with it.

2 So --

3 MR. BECK: Your Honor --

4 MS. MARCUS: -- reflect that.

5 THE COURT: Sorry?

6 MS. MARCUS: This is Jacqueline Marcus again. I
7 was just wondering how you would want us to reflect that.

8 THE COURT: I can just add it to the so-ordered
9 line.

10 MR. BECK: And, Your Honor, I just wanted to
11 clarify (indiscernible). There is no agreement
12 (indiscernible) to purchase (indiscernible) sort of --

13 THE COURT: Sorry, you're --

14 MR. BECK: -- or agreement.

15 THE COURT: You're cutting in and out. If you
16 could just repeat that, please.

17 MR. BECK: Sure, Your Honor. (indiscernible) that
18 there's no current agreement between Broe (indiscernible)
19 entity right now. (indiscernible) still very
20 (indiscernible) in purchasing the parking lot in the future
21 and will continue to try to do so, but that is an arm's
22 length transaction and there is no sort of (indiscernible).

23 THE COURT: Right. And that's all I -- that's all
24 I'm focusing on. If down the road, Broe purchases the
25 parking lot, that's fine. I just want to make sure that

1 there's no agreement today that -- or understanding that
2 that purchase is going to happen, because obviously that
3 would be collusive with respect to the bidding. But
4 obviously, if they get back together again or they get
5 together again six months from now or three months from now
6 or two months from now and negotiate a new agreement, that's
7 fine.

8 MR. BECK: (indiscernible).

9 THE COURT: Okay. So I'll just -- Ms. Marcus, you
10 sent me the -- you or someone at Weil sent me the proposed
11 stip yesterday. I'll just add that condition to the so-
12 ordered line.

13 MS. MARCUS: Okay, perfect. Thank you, Your
14 Honor.

15 THE COURT: And I don't know, did you also send
16 the order approving the sale?

17 MS. MARCUS: So we don't believe we need an order
18 approving the sale --

19 THE COURT: Okay.

20 MS. MARCUS: -- asset procedures. We're
21 authorized to proceed if any objection is withdrawn so the
22 stipulation is withdrawing the objection and therefore, we
23 don't think we need a separate order approving the sale.

24 THE COURT: All right. That's fine. Very well.
25 So, and again, to the extent that's an issue, I'm approving

1 the sale.

2 MS. MARCUS: Thank you, Your Honor.

3 THE COURT: Okay.

4 MR. DIDONATO: Good morning, Your Honor. This is
5 Phil DiDonato from Weil, Gotshal, and Manges on behalf of
6 the Debtors. The next item on the agenda, No. 5, are the
7 motions of Julie Tomchak and there are actually two motions
8 going forward here today, the original filed at ECF No. 4209
9 and the addendum that was filed at ECF No. 5483. Our
10 understanding is that both of these motions related to the
11 same underlying claim. I'll note that these were not filed
12 formally as motions to release the automatic stay, but we
13 treated them as such in our response because they relate to
14 a prepetition claim against the Debtors.

15 Our objection is filed at ECF No. 7475 and today
16 we're asking that the Court reject these motions, that these
17 motions be denied for the reasons stated in our objection,
18 namely that there's no insurance available to this claim.

19 THE COURT: Okay. And when you say there's no
20 insurance available, you mean literally the policy limits
21 for the first tier coverage have not been -- they've been
22 exceeded and the coverage has been exhausted at this point,
23 correct?

24 MR. DIDONATO: That's correct.

25 THE COURT: And then as far as any excess coverage

1 is concerned, the excess coverage is only for claims over
2 and above \$5 million and this claim, as asserted, is in the
3 thousands of dollars range as opposed to over \$5 million?

4 MR. DIDONATO: Correct.

5 THE COURT: Okay. Is Ms. Tomchak on the phone?
6 She had sought to have this --

7 MS. TOMCHAK: Yes.

8 THE COURT: -- be a telephonic hearing.

9 MS. TOMCHAK: Yes, I am here.

10 THE COURT: Okay. Good morning. I had one
11 question for the Debtors, which is, as I read Ms. Tomchak's
12 motion, she really wants to go against the insurer. The
13 Debtors have represented, and I accept, that there is no
14 insurance coverage that's available. She also says,
15 however, that the insurer prepetition wrongfully denied her
16 claim. Do the Debtors object to lifting the stay solely as
17 to Ms. Tomchak proceeding against the insurer for wrongful
18 denial?

19 MR. DIDONATO: So, Your Honor, I don't think we
20 have any issue with that. The real issue here was just
21 (indiscernible) the automatic stay to proceed against the
22 Debtors here.

23 THE COURT: Right. And as I read it --

24 MR. DIDONATO: I don't think --

25 THE COURT: -- Ms. Tomchak really doesn't want to

1 proceed against the Debtors, per se, because her real beef
2 is that the insurer turned down her request to pay out,
3 prepetition.

4 MS. TOMCHAK: The issue was -- yes. There was a
5 third party which was (indiscernible) they are actually not
6 the insurer. They are supposed to be a third party that
7 passes it along to the insurance company and apparently a
8 week before Sears filed for bankruptcy, they chose to throw
9 in everything, even though I had been waiting a year to
10 process this already, they decided to throw it into the
11 bankruptcy so that they would not have to pay out.

12 THE COURT: Right, but that third party would be
13 the agent for the insurer. That's the adjustor for the
14 insurer.

15 MS. TOMCHAK: So, is --

16 MR. FAIL: Your Honor, I'm not sure if that's
17 correct.

18 THE COURT: Okay.

19 MR. FAIL: Your Honor, this is Garrett Fai. I'm
20 not sure that that's correct, that they're the agent for the
21 insurer as opposed to agents for the Debtors. I'm just --
22 I'm not sure that that's right. I don't know the facts, but
23 I don't know that it's correct that they are an agent for
24 anyone other than the Debtor. I'm also not sure that
25 there's a direct claim against (indiscernible).

1 THE COURT: Well, there may not be --

2 MR. FAIL: -- for anything --

3 THE COURT: There may not be. There may not be a
4 direct claim against the insurer, but as long as that claim
5 doesn't come back to bite the Debtor, I don't see a basis
6 for the Debtor being hurt by lifting the stay. Now, the
7 third party we're referring to is Sedgwick Claims Management
8 Services as third party administrator.

9 MS. TOMCHAK: Correct.

10 THE COURT: So it is possible that they -- I mean,
11 it says, their letter says, "Sedgwick Claims Management
12 Services as third party administrator manages claims for
13 Sears Roebuck and Company on behalf of Ace American
14 Insurance Company." So my thought would be that the stay
15 would be lifted solely to the extent that Ms. Tomchak wants
16 to pursue a claim against Ace American Insurance Company
17 and/or Sedgwick solely in its capacity, if any, as agent for
18 Ace for wrongful denial of coverage, there being no
19 representation that there is such a direct claim.

20 And there may well not be, Ms. Tomchak. I'm not
21 saying that there is, either as a matter of law that there's
22 a direct right for denial of coverage that you would have or
23 as matter of the facts, that they wrongfully denied the
24 coverage. So you might be pursuing this for no reason, but
25 the point would be that there would be no claim over against

1 the Debtor and the litigation would have to stop if it
2 appeared that either Ace or Sedgwick would have a claim over
3 against the Debtor.

4 MS. TOMCHAK: At this point, I was told by
5 Sedgwick that I had to go against Sears. That's what I was
6 instructed.

7 THE COURT: Well, if you have a claim against
8 Sears, that's correct. But if you have an independent claim
9 against the insurer or Sedgwick for wrongfully denying
10 coverage, directly, a direct claim that you would have that
11 didn't affect Sears, then you could go against them;
12 although, again, I don't know whether that's true as a
13 matter of law.

14 MS. TOMCHAK: I am not exactly sure on that. All
15 I know is when I have actually called, like, my insurance
16 company or someone who deals with insurance and people going
17 through bankruptcy, I was told that they had to handle every
18 insurance claim within a timely manner and this has gone on
19 longer than, what, two years, three years. And so it was
20 not handled in a time-appropriate manner which is the
21 national law. It doesn't apply to this one state. It's a
22 nationwide --

23 THE COURT: Well --

24 MS. TOMCHAK: -- that was my frustration.

25 THE COURT: Look, I don't know whether that is

1 true as a matter of law or fact, but what I'm saying is the
2 following, and I appreciate it's a fairly arcane aspect of
3 bankruptcy law. First, this is something basic to
4 bankruptcy law. The automatic stay is in the statute. It
5 comes into effect when a company files bankruptcy. It means
6 that unless you get relief from the automatic stay on a
7 motion filed with the Court, you can't proceed against the
8 Debtor, in this case, Sears.

9 And it's true that if your claim to the insurance
10 is based on a claim against Sears, you can't proceed against
11 the insurance until you get relief from the automatic stay
12 in the bankruptcy case.

13 MS. TOMCHAK: Okay.

14 THE COURT: It is fairly common where --

15 MS. TOMCHAK: Okay.

16 THE COURT: Let me just -- because there's a
17 second element in this. It's fairly common in bankruptcy
18 case when someone moves for relief from the stay and says, I
19 only want to go against the insurance and the Court
20 determines that that will adversely affect the Debtor, the
21 Court will lift the automatic stay so that a party can go
22 against the insurance only, and there are a lot of
23 stipulations and order in this case that, where there is
24 insurance, the stay has been lifted.

25 But here, the Debtors say there is no insurance.

1 It's all been used up. So that avenue is closed to you
2 because it would be a waste of everyone's time, including,
3 importantly, yours to agree to lift the stay to go against
4 insurance when there's no insurance. The --

5 MS. TOMCHAK: Yeah.

6 THE COURT: The different thing about your motion
7 is that you're basically saying they should've honored my
8 claim, the insurer should have, prebankruptcy and they
9 didn't. So I'm saying, I would not -- I would enter an
10 order lifting the stay to the extent you have a cause of
11 action, a direct cause of action, against the insurer or its
12 agent for wrongful denial of coverage. I don't know whether
13 you have such a direct cause of action, but it doesn't
14 affect -- it wouldn't affect the Debtor.

15 So I would lift the automatic stay to permit you,
16 if you wanted to, to go against the insurer and/or its
17 agents if you can show that they wrongfully denied the
18 coverage and it's a direct claim against the insurer. The
19 lawyer then -- you'd have to hire a lawyer to go do that,
20 and I don't know whether that would win or not or whether
21 the lawyer would tell you you're wasting your money in
22 paying me, but I'm prepared to lift the stay to let that
23 happen.

24 MS. TOMCHAK: Okay. (indiscernible).

25 THE COURT: Okay, so I'm going to ask the Debtors

1 to prepare that order which, again, doesn't lift the stay to
2 let you go to sue the Debtor either directly or indirectly.
3 It just permits you, if you have a direct action against the
4 insurer for wrongful denial of coverage and/or the insurer's
5 agent, to go and do that.

6 MS. TOMCHAK: Okay.

7 THE COURT: But you have to be really careful not
8 to name the Debtor as someone that you're asserting a claim
9 against, that you're pursuing a claim against the Debtor,
10 because that would violate the stay and subject you to
11 sanctions. So you have to be really clear. The order will
12 be clear. When you go and hire a lawyer, if you decide to
13 do that, you need to show that person the order so that they
14 will know not to get you in trouble by drafting a complaint
15 that will seek relief from the Debtor, either directly or
16 indirectly.

17 MS. TOMCHAK: I see. Okay.

18 THE COURT: Okay? All right. So that order will
19 be entered fairly soon on the docket. You should look for
20 it and then you can print it out and give it to a lawyer if
21 you want to hire a lawyer to pursue it.

22 MS. TOMCHAK: Okay. Thank you.

23 THE COURT: Okay, very well. Okay, before we get
24 to the first matter on the agenda, there are a number of
25 adjourned matters on the agenda as well as some withdrawn

1 matters. I don't know if the Debtors wish to make any sort
2 of report in connection with any of the adjourned matters.
3 I'm not telling you, if you're not -- if that's not
4 something that you had prepared to do. But if you had
5 prepared to give a status update, generally or any of these
6 particular matters, you should feel free to do so now.

7 MR. FAIL: Thank you, Your Honor. Garrett Fail,
8 Weil, Gotshal, and Manges. There is no update prepared.
9 This was a notice only, but appreciate the opportunity.

10 THE COURT: Okay. So why don't we return, then,
11 to the first matter on the agenda. I don't think there's
12 anything else left other than that, correct, which is VIR
13 Ventures, Inc.

14 MS. KRAEMER: -- Your Honor.

15 THE COURT: -- versus Sears? I had been passed a
16 note that Ms. Kraemer, the plaintiff's counsel, was logging
17 on late to the phone. Are you on now, ma'am?

18 MS. KRAEMER: Your Honor, I'm here.

19 THE COURT: Okay, good. All right. Well, you
20 didn't miss anything because we put this at the end, given
21 that it would take the longest. So what is on the calendar
22 in this adversary proceeding, VIR Ventures, Inc. and AMI
23 Ventures, Inc. v. Sears Holdings Corp. et al., is the
24 Debtors' motion to dismiss what I believe are the remaining
25 causes of action in the complaint and you should assume that

1 I've read the pleadings on this and gone through it.

2 I do want to just confirm, we had a hearing a
3 couple of weeks ago on a related VIR Ventures/AMI Ventures
4 matter in which I stated that the other causes of action in
5 the complaint, that is other than the ones that are subject
6 to this motion, should be treated as dismissed because
7 they're in derogation of Bankruptcy Rule 7001 and I haven't
8 seen an order on that, but is there any dispute about that
9 at this point?

10 MS. KRAEMER: No, Your Honor.

11 THE COURT: All right.

12 MS. CROZIER: No, Your Honor, there is not.

13 THE COURT: All right. So we're focusing on the
14 causes of action that are the subject of the motion which
15 are count two for express trust or the imposition or
16 declaration of an express trust, count four for the
17 imposition of a constructive trust based on the allegations
18 in the complaint generally, and then to the extent not tied
19 to a breach of contract claim, count five for unjust
20 enrichment.

21 So it's the Debtors' motion, so I should hear from
22 them first, to the extent they want to have any oral
23 argument as opposed to just resting on their papers.

24 MS. CROZIER: Thank you, Your Honor. This is,
25 again, Jennifer Crozier, Weil, Gotshal, and Manges, for the

1 Debtors. Again, thank you for your time this morning, and
2 given the circumstances, I do intend to be brief.

3 We respectfully request that the Court dismiss the
4 remaining counts of plaintiffs' complaint which we
5 understand to be, as you just said, the breach of express
6 trust, constructive trust, and to the extent not predicated
7 on the already dismissed counts, that the claim for
8 conversion.

9 As the Bankruptcy Court for the Southern District
10 of New York stated in the In RE: Ames Department Stores
11 (indiscernible) trust or agency to a contract does not,
12 without more, convert an ordinary (indiscernible) into a
13 trust or agency relationship. Where (indiscernible) rights
14 for creditors are at issue, it is (indiscernible) important
15 that substance not give way to form. We must look to the
16 parties' actual (indiscernible) the status of the property
17 at issue.

18 The relative rights (indiscernible) other
19 creditors are implicated here, Your Honor, and therefore, we
20 must look to the substance of the relationship between
21 plaintiffs and the Debtors in order to determine the status
22 of the property at issue in this case whether it's
23 (indiscernible) purported trust or, in fact, part of the
24 Debtors' estate.

25 Now, according to the plaintiffs themselves, the

1 business relationship between plaintiffs and the Debtors had
2 none of the hallmarks of a trust relationship. Plaintiffs
3 themselves that the Debtors exercised control over the sale
4 proceeds, comingled them with their own funds, and used them
5 for their own purposes. Plaintiffs themselves have alleged
6 a Debtor-creditor relationship and accordingly, and for all
7 the other reasons that we've set forth in our papers, the
8 Court should dismiss plaintiffs' breach of express trust
9 claims.

10 The Court should likewise dismiss plaintiffs'
11 claims for imposition of a constructive trust. Among other
12 things, plaintiffs have failed to adequately allege any
13 wrongdoing on the part of the Debtors that would warrant the
14 imposition of such an extraordinary remedy. Plaintiffs
15 allegations of wrongdoing, again, as we argue in our papers,
16 are bare, conclusory, and fail to satisfy the proving
17 standard set forth in Rule 9(b). The same is true for the
18 (indiscernible) improper allegations plaintiffs assert in
19 their opposition which, again, as the Debtors argue in their
20 reply, the Court should not consider in adjudicating the
21 plaintiffs' motion to dismiss.

22 And finally, Your Honor, the Debtors respectfully
23 request that the Court dismiss plaintiffs' claim for
24 conversion which is premised entirely upon the dismissed
25 breach of contract claims. One need only look at Paragraph

1 133 to 135 of the complaint to see that and each of those
2 explicitly referenced the Sears (indiscernible) agreement
3 and the Debtors' alleged failure to perform pursuant to
4 those agreements, and even if the conversion claim were not
5 based on the dismissed contract claim which the Debtors
6 don't concede, it would be barred by the economic loss
7 doctrine as recognized in Illinois.

8 So in sum, Your Honor, as the Third Circuit
9 (indiscernible) in In RE: Morales Travel Agency which is
10 cited by the (indiscernible), if a ritualistic incantation
11 of trust language conclusive where third-party interests are
12 at stake in a bankruptcy case, it would be a simple matter
13 for one creditor, at the expense of others, to circumvent
14 the rules pertaining to the creating of bona fide security
15 interests.

16 As the Debtors have argued (indiscernible) of this
17 adversary proceeding, Your Honor, that's precisely what
18 plaintiffs have attempted to do here and the Debtors submit
19 that the Court should not permit plaintiffs to sidestep the
20 procedures approved by this Court for the orderly and
21 efficient resolution of administrative expense claims and
22 thus we respectfully ask the Court to dismiss the remaining
23 counts of this adversary complaint with prejudice. I'm
24 happy to answer any questions Your Honor may have;
25 otherwise, I'm finished.

1 THE COURT: Okay, thank you.

2 MS. CROZIER: Thank you so much.

3 THE COURT: Okay. Ms. Kraemer?

4 MS. KRAEMER: Yes, Your Honor, thank you. Your
5 Honor, we would respectfully request that this motion to
6 dismiss be denied. We feel as though that the motion to
7 dismiss is premature, particularly in light of the fact that
8 we've had no discovery in this case. While we have asked
9 for a notice of a 30(b)(6) deposition, we have not been able
10 to obtain that.

11 THE COURT: Well, that's --

12 MS. KRAEMER: -- Your Honor --

13 THE COURT: I'm sorry, that's why you have a
14 motion to dismiss, is so that the -- if it can be granted,
15 the defendant doesn't have to incur the burden and expense
16 of discovery.

17 MS. KRAEMER: I agree, Your Honor. We still take
18 the position that this motion is premature. We also believe
19 that it is -- the Debtors have not satisfied their burden
20 for a motion to dismiss, Your Honor. We believe that this
21 issue is a novel one and a case of first impression with
22 respect to e-marketplace portals that are relatively new to
23 the retail industry. We believe that our complaint does
24 satisfy and sufficient plead (indiscernible) claims for at
25 least, Your Honor, for a constructive trust.

1 We believe that the evidence would reveal, and we
2 have pled in our pleadings specific representation by Sears
3 customer representatives that -- and based on information
4 that has come to light since we filed the complaint, that
5 this, perhaps, is a system-wide fraudulent scheme, if not
6 fraudulent definitely mistaken where customer
7 representatives intentionally misinformed the plaintiffs as
8 well as -- I had no idea the numerous e-marketplace
9 following.

10 Your Honor, we believe that with respect to --
11 indulge me one second. With -- I'll address the
12 constructive trust directly, Your Honor. Again, we feel as
13 though that the facts here are sufficient so that the
14 wrongdoing here that we believe were perpetrated upon my
15 clients, it should be that a constructive trust is an
16 equitable remedy that once one in this situation, we believe
17 that the five-year relationship between my clients and the
18 representatives built a high degree of trust and that at the
19 time that these representations were made to my clients,
20 they were made intentionally, we believe, by the
21 representatives to ensure that my clients would continue to
22 do business with Transform and with Sears.

23 And we believe that the express language of the
24 agreement created a fiduciary duty on behalf of Sears as an
25 agent, if not as a trustee to a constructive trust to have

1 not used that money for its own purposes and that they
2 should have -- and because it was money of the customers'
3 and not my clients, we believe that this was a unique kind
4 of relationship and not your typical Debtor-creditor
5 relationship.

6 Your Honor, we have expressly pled in the
7 pleadings, the emails that were sent back and forth to my
8 client by Brian Carr, and we see that certain of the
9 messages that were sent could be considered future
10 statements that we hold or we anticipate, but we believe
11 that certain statements were statements that are present
12 statements. For example, Your Honor, that on October 15th,
13 2018, Brian Carr stated that message, he indicated, business
14 would be -- payments would be restarting.

15 Your Honor, Brian Carr also stated that per the
16 contract, this is lawfully obligated and cannot be set up or
17 closed down and payments are guaranteed. Your Honor, Brian
18 Carr also stated that marketplace sellers are sellers and
19 not vendors which allow you to be in a distinct class, you
20 ahead of other creditors. You should start receiving
21 payments regular, post October 15th payments by next week.

22 Your Honor, in an email on Tuesday, February 12th,
23 he states that, as of yesterday it appears we are officially
24 out of Chapter 11. Your Honor, we respectfully submit that
25 if these aren't tantamount to fraud, they're definitely

1 mistaken. They were negligent and as a result -- and I
2 believe that these statements were made to e-marketplace
3 sellers across the board, and that this would be considered
4 a scheme, in our opinion, so more e-marketplace sellers
5 continued to do business.

6 Your Honor, for all of these reasons, I would
7 respectfully request that the motions for dismiss be denied
8 and that equity and good conscience would require it.

9 THE COURT: Okay. I have the so-called Sears
10 Marketplace Agreement under which the parties conducted
11 their business. It's referred to an incorporated in the
12 compliant. Based on my review of it, there is one paragraph
13 in the agreement that refers to an agency relationship which
14 is quoted in the complaint. It's Paragraph 1(b) and it says
15 that, "Seller hereby appoints Sears as an agent of seller
16 for the sole and express purpose of receiving payments form
17 users for seller's merchandise sold on the websites."

18 I don't see any other agency language, so my first
19 question is, is there any other express agency language in
20 the agreement besides that paragraph?

21 MS. KRAEMER: No, Your Honor, that is it.

22 THE COURT: Okay. And then the second question I
23 have is, is there any language in the agreement, including
24 in that paragraph, laying out how or even whether the
25 seller, namely your clients, have the right and ability to

1 control Sears in how it performs its work as agent?

2 MS. KRAEMER: I'm sorry, Your Honor, you mean,
3 with respect to Sears as agent for my clients?

4 THE COURT: For your client, yes.

5 MS. KRAEMER: Or --

6 THE COURT: Sears as agent for your client.

7 MS. KRAEMER: With respect to control over the
8 funds or just control over --

9 THE COURT: Any control, as agent. Is there any
10 provision whereby the sellers are given control over Sears'
11 actions?

12 MS. KRAEMER: So just to be clear, so my clients'
13 ability to control what Sears does with the money or vice
14 versa? I'm confused.

15 THE COURT: No, I'm just focusing on their control
16 over Sears. Normally, a principal has the right to control
17 its agent, if there's a true --

18 MS. KRAEMER: Okay.

19 THE COURT: -- agency relationship.

20 MS. KRAEMER: Okay. Well, with respect to the
21 transaction, I know that -- and my client was in a very
22 vulnerable -- as a principal relationship here, in a very
23 vulnerable position because once the customer orders the
24 treadmill off of Sears, my client was contractually
25 obligated to go out and find that product and then deliver

1 it to the customer and then my client would only -- but
2 Sears would collect the credit card funds once the customer
3 made the transaction, and my client had -- really had no
4 control over Sears.

5 They had control over obtaining the treadmill,
6 having it delivered to a third party, and having proof of
7 delivery, then sent to Sears, and then upon that proof of
8 delivery, Sears was then supposed to remit the funds,
9 including taxes (indiscernible) authorities. That is my
10 understanding, there's about \$40,000 of taxes that have not
11 been remitted properly. But in terms of a control, Sears
12 really had control over the funds and -- once that customer
13 issued the credit card payment.

14 Sears -- yeah, and Sears, my client was not
15 permitted to, for marketing purposes, have any type of
16 marketing materials on the packaging that was ultimately
17 sent to the customer, so I know I'm not really answering
18 your question, but in this kind of a situation, my client
19 didn't have that much control. They're in a vulnerable
20 position. It's a novel kind of way to do business, and I've
21 asked my clients why is this the industry standard, why are
22 e-marketplace sellers -- this contract needs to be
23 rewritten.

24 The 503(b)(9) doesn't help us much at all and this
25 leaves them all exposed and vulnerable, particularly in

1 these recall cases. So that's my answer. I don't have any
2 -- not sure what else I could say about that.

3 THE COURT: Okay. And as I read it, Sears has no
4 responsibility to immediately pay the money over, right?

5 MS. KRAEMER: They were to pay the money within 15
6 days after proof of shipment.

7 THE COURT: Right.

8 MS. KRAEMER: And they were also obligated to
9 remit the taxes, too.

10 THE COURT: Right. Was there any timeframe for
11 that?

12 MS. KRAEMER: for the taxes? That was set forth
13 in Paragraph 48 of the complaint. That's the contractual
14 language. It doesn't say. It just says, Sears will pay
15 over taxes collected from the online purchaser directly to
16 the seller and seller will be responsible for remitting,
17 except in states where Sears as the marketplace
18 (indiscernible) provider is either required by law or elects
19 to remit those taxes to the state on behalf of the seller.
20 I do not see a see (indiscernible) here.

21 THE COURT: Okay.

22 MS. KRAEMER: (indiscernible). Yeah. It says,
23 seller will promptly reimburse Sears for any amounts paid --

24 THE COURT: Right.

25 MS. KRAEMER: -- to the extent that

1 (indiscernible) Sears to pay any of the seller's taxes.

2 THE COURT: Okay. And I didn't see any -- I mean,
3 I think that's the operative language in the agreement that
4 you quoted in Paragraph 48.

5 MS. KRAEMER: That's right.

6 THE COURT: Right, which is Paragraph IIb3.

7 MS. KRAEMER: Your Honor, if I may, this agreement
8 is -- we would think of it as a contract of adhesion. It
9 wasn't an agreement that was --

10 THE COURT: Well, but --

11 MS. KRAEMER: -- format. Each e-marketplace
12 seller would --

13 THE COURT: But, no, that's not -- Ms. Kraemer,
14 that's not alleged in the complaint so it's really not an
15 issue that's before me.

16 MS. KRAEMER: Okay.

17 THE COURT: Okay, anything else?

18 MS. KRAEMER: (indiscernible). We allege, for the
19 constructive trust, I note it in Illinois, the earmarks are
20 mistake, fraud, coercion, or duress, and I guess that's
21 where I'm going with that, because Sears as a
22 megacorporation and then these small e-marketplace sellers -
23 -

24 THE COURT: But you haven't alleged --

25 MS. KRAEMER: -- there's really no --

1 THE COURT: But Ms. Kraemer, you haven't alleged
2 any duress.

3 MS. KRAEMER: Your Honor, we did in the complaint.
4 We did (indiscernible) constructive trust part.

5 MS. CROZIER: Your Honor, if I may, this is
6 Jennifer Crozier for the Debtor. My line went dead for a
7 moment. But if I may address Ms. Kraemer's argument
8 concerning this being a contract of adhesion or duress --

9 THE COURT: Well, but please let's just finish
10 this thought. I didn't see allegations of duress or
11 adhesion here.

12 MS. KRAEMER: Your Honor, if I may --

13 MS. CROZIER: -- and in fact, plaintiffs have
14 alleged quite the opposite. They have alleged at Paragraph
15 21 that they are, "longstanding e-marketplace sellers." At
16 28, they have alleged that they are likely one of Sears' top
17 marketplace sellers that provide the largest selection and
18 number of different products for Sears to sell and together
19 provide at least one million unique SKUs. They have not
20 alleged that they are the little guy against the big guy.
21 They haven't alleged that.

22 And to the extent that they're relying on Brian
23 Carr's statement to show that they reposed confidence in
24 anyone, they must allege that they reposed confidence in
25 someone with respect to the execution of the Sears

1 marketplace agreements and they have not done that. Their
2 relationship with Brian Carr alleges they began in 2013.
3 That's at Paragraph 54. And AMI, at least, entered into its
4 contract in 2010. So there are no allegations of adhesion
5 or duress. Certainly, we have no fiduciary duty here, at
6 least no adequate allegations under Trombe or Iqbal, and in
7 fact, their allegations would suggest the opposite.

8 THE COURT: Okay, Ms. Kraemer --

9 MS. KRAEMER: Your Honor, if I may.

10 THE COURT: Yeah, you were going to show me
11 allegations of duress here.

12 MS. KRAEMER: Yes, Your Honor. It's in the
13 constructive trust count, Your Honor, and it's Paragraph 118
14 to 126. I'd say that -- specifically I'd say that in
15 Paragraph 120, Sears (indiscernible) retail powerhouse
16 (indiscernible) tower in dominion over plaintiffs as well as
17 other e-marketplace sellers. There was a longstanding
18 relationship with sellers and a high degree of trust between
19 Rupeshi Sanhavi and Pankaj Rothi empirically (indiscernible)
20 akin to a confidential relationship. Certain of its
21 statements to plaintiff were mistaken, if not outright
22 false.

23 There was a market disparity and this is
24 experienced between the plaintiffs who were not represented
25 by counsel in Sears, that plaintiffs trusted Carr. The

1 plaintiffs were under commercial duress after the petition
2 date because of the large unpaid prepetition sums which were
3 about \$880,000, Your Honor. These compelling facts support
4 a basis of a constructive trust.

5 And the margins -- just to you know, Your Honor,
6 the margins on, like for an \$800,000 of goods that my
7 clients purchased and delivered to customer funds and then
8 those funds were then -- Sears would take the funds. Sears'
9 commission is dependent upon the product that was delivered,
10 but it would be, like, 3 percent, 5 percent, 10 percent, and
11 then my clients' margins on these products were varied.
12 They said it was like 1 percent. They're very slim margins,
13 so for Sears to take all the monies that should've been used
14 to actually purchase the product and provide the product, I
15 mean, my clients are -- it's a huge hit on someone like my
16 clients.

17 It's a small business. They do a lot of business.
18 They did so a lot of business with Sears, but it's...

19 THE COURT: So let me -- the allegedly false
20 representations are all post-petition, correct?

21 MS. KRAEMER: I'm sorry, can you repeat that?

22 THE COURT: I think, based on my reading of the
23 complaint, the allegedly fraudulent representations by Mr.
24 Carr are all post-petition, after the commencement of the
25 bankruptcy, correct?

1 MS. KRAEMER: Your Honor, if you look at page --
2 it was on the petition date, was the first email --

3 THE COURT: Right, so --

4 MS. KRAEMER: -- 11.

5 THE COURT: So post-petition?

6 MS. KRAEMER: That was on the petition date.

7 THE COURT: Right. So I guess this is a
8 subsidiary point, but I didn't understand how that could
9 justify imposing a constructive trust for the whole \$790,000
10 of prepetition amounts.

11 MS. KRAEMER: Your Honor, I understand that and I
12 have thought about that and I did digest this. At what
13 point were these statements made, and I asked them were
14 there any other statements prior to this date, like -- that
15 were like this. The answer is no.

16 THE COURT: Okay.

17 MS. KRAEMER: So there were -- the analysis, I
18 think, with respect to the constructive trust, it would have
19 to come after the date that these statements were made and
20 there were prepetition -- in the 20 days, I know the number
21 is like \$800,000-and-some or \$700,000-and-some, and then the
22 post-petition, I know there's an amount that -- and Jennifer
23 and I have discussed this amount -- it's about, we think
24 it's, I think, \$100,000. They think it's about \$75,000. So
25 --

1 THE COURT: Well, the compliant says it's 95.

2 MS. KRAEMER: Yeah, then when we were trying to
3 resolve our -- through administrative claims consent
4 program, there were some issues about duplicative invoices
5 or refunds or whatever. We're really not -- didn't get to
6 the nitty gritty of that, but the Debtors believe that the
7 number is 75. My clients thought it was 95.

8 THE COURT: Okay. All right. Very well.
9 Anything else?

10 MS. KRAEMER: I have nothing further, Your Honor.

11 THE COURT: Okay. Anything else from the Debtors'
12 side?

13 MS. CROZIER: Nothing further here, Your Honor.
14 Thank you.

15 THE COURT: Okay. All right. I have before me a
16 motion by the Debtor defendants in this adversary proceeding
17 to dismiss the agreed remaining claims in the adversary
18 proceeding, which are counts two, four, and to the extent
19 that the counts set forth in V is for conversion unrelated
20 to a breach of the parties' contract, count five, under
21 Bankruptcy Rule 7012 which incorporates Federal Rule of
22 Civil Procedure 12(b)(6).

23 When considering a motion under Rule 12(b)(6), the
24 Court must assess the legal feasibility of the complaint,
25 not weigh the evidence that might be offered in its support.

1 Koppel v. 4978 Corp., 167 F.3d. 125, 133 (2d Cir. 1993).

2 The court's consideration is limited to facts stated on the
3 face of the complaint and the documents appended to the
4 complaint or incorporated in the complaint by reference as
5 well as to matters of which judicial notice may be taken.

6 Hertz Corp. v. city of New York, 1F.3d. 121, 125, (2d. Cir.,
7 1993, cert., denied), 510 U.S. 1111 (1993).

8 The Court accepts the complaint's factual
9 allegations as true and must draw reasonable inferences in
10 favor of the plaintiff. Tellabs, Inc., 551 U.S. 308, 323
11 (2007). However, if a complaint's allegations are clearly
12 contradicted by documents incorporated into the pleadings by
13 reference, the Court need not accept them. Labajo v. Best
14 Buy Stores, LP, 478 F. Supp. 2d 523, 528 (SDNY 2007).

15 Moreover, the Court is not bound to accept as true
16 a legal conclusion couched as a factual allegation. Papasan
17 v. Allain, 478 U.S. 265, 286 (1986). Instead, the complaint
18 must state more than "labels and conclusions and a formulaic
19 recitation of the elements of the cause of action will not
20 do." Bell Atlantic Corp. v. Twombly, 550 U.S. 544, 555
21 (2007).

22 Relatedly, while the Supreme Court has confirmed
23 in light of the notice pleading standard of Federal Rule of
24 Civil Procedure 8A that a complaint does not need detail
25 factual allegations to survive a motion under Rule 12(b)(6),

1 see Erickson v. Pardus, 127 Supreme Court 2197, 2200 (2007);
2 Bell Atlantic Corp. v. Twombly, 550 U.S. at 555. Its
3 "factual allegations must be enough to raise a right to
4 relieve above the speculative level." Bell Atlantic Corp.
5 v. Twombly at 555.

6 Complaint must contain sufficient facts except it
7 is true to state a claim that is "plausible on its face",
8 id. at 570. In other words, if the claim would not
9 otherwise be plausible on its face, the plaintiff must
10 allege sufficient facts to "nudge the claim across the line
11 from conceivable to plausible," id., otherwise the defendant
12 should not be subjected to the burdens of discovery and the
13 worry of overhanging litigation, id.

14 Evaluating plausibility is "a context-specific
15 task that requires a Court to draw on judicial experience
16 and common sense, aware that well pleaded facts to not
17 permit the Court to infer more than mere possibility of
18 misconduct the complaint has alleged but has not shown that
19 the pleader is entitle to relief under Rule 8." Ashcroft v.
20 Iqbal, 129 Supreme Court 1937, 1949 (2009).

21 The plausibility standard is not akin to a
22 "probability requirement" but it asks for more than sheer
23 possibility that the defendant has acted unlawfully, id.

24 In sum, therefore, to determine this motion to
25 dismiss, the Court must first identify the elements of the

1 applicable causes of action, id. at 1947. Next, it must
2 identify the allegations not entitled to the assumption of
3 truth because they are legal conclusions, not factual
4 allegations, id. at 1951. And finally, it must assess the
5 factual allegations in the context of the elements of the
6 claim to determine whether they plausibly suggest an
7 entitlement to relief, id.

8 The motion also is couched to the extent that the
9 causes of action at issue are premised upon allegations of
10 fraud on Rule 9 of the Federal Rules of Civil Procedure
11 incorporated by Bankruptcy Rule 7009. That rule requires
12 wherever fraud is alleged that with respect to allegations
13 other than state of mind, the allegations be stated with
14 particularity as to the circumstances constituting fraud,
15 which is morally interpreted to state that the alleged fraud
16 must be stated with particularity as to the who, what,
17 where, and when aspects of the fraud, so that the defendant
18 is not asked in its answer to speculate or guess as to the
19 circumstances pertaining to the alleged fraud.

20 Here, again, there are three causes of action that
21 are the subject of the motion. The first is a cause of
22 action for a declaration of express trust between the
23 parties. The parties do not have an agreement which
24 declares expressly a trust. Rather, their relationship, as
25 set forth in the complaint, is under a so-called Sears

1 Marketplace agreement, which, since it is referred to in the
2 complaint and incorporated therein, as I noted above, I can
3 consider.

4 Whether parties have an expressed declaration of
5 trust or not, however, is not dispositive as to whether they
6 have agreed to such an express trust. Rather, under
7 Illinois law, which is the law that the parties, I believe,
8 agree applies here, and in any event, which they have agreed
9 applies with respect to their relationship under the Sears
10 Marketplace agreement in paragraph F thereof, the creation
11 of an express trust requires each of the following elements
12 to be established. That is, the complaint here would have
13 to plead sufficiently under Twombly and Iqbal the following:

14 "Intent of the parties to create a trust, which
15 may be shown by a declaration of trust by the settler or by
16 circumstances which show the settler intended to create a
17 trust; 2) A definite subject matter or trust property; 3)
18 Ascertainable beneficiaries; 4) A trustee; 5) Specifications
19 of a trust purpose and how the trust is to be performed; and
20 6) Delivery of the trust property to the trustee." See
21 Eychaner v. Gross, 779 N.E.2d 1115, 1131, (Ill. 2002).

22 Here, as I said, the agreement between the parties
23 does not refer to a trust relationship and the complaint
24 itself does not refer to any agreement whereby the parties
25 denominated their relationship as one subject to an express

1 trust. Indeed, paragraph G of the agreement states: "The
2 parties to this agreement are independent contractors and no
3 other relationship will be implied from this agreement."

4 In fact, the only statement of agency in the
5 agreement is the one that we discussed at oral argument
6 appearing in paragraph 1B, which states: "Seller hereby
7 appoints Sears as an agent of Seller for the sole and
8 express purpose of receiving payments from users for
9 Seller's merchandise sold on the websites. Unlimited
10 declaration of agency."

11 In addition, it is not clear from the complaint
12 what the subject matter or trust property is, although I
13 have inferred that it is the cash received by Sears in
14 respect of sales of merchandise sold under the Sears
15 Marketplace terms and conditions on its website provided by
16 the Plaintiffs as sellers. That's with an under-case S
17 under the marketing agreement.

18 Each of the other aspects of finding an express
19 trust, i.e., ascertainable beneficiaries, a trustee,
20 specifications of a trust purpose and how the trust is to be
21 performed and delivery of the trust property to the trustee
22 are not delineated expressly in the complaint. And, again,
23 I have to infer that each of those requirements is intended
24 to be satisfied by the delivery of the payments by those who
25 order merchandise to Sears, ostensibly to be held in trust

1 for the Plaintiffs, although there's no allegation, and this
2 really does cross the line of Twombly/Iqbal, to suggest that
3 the customers making the payments to Sears had any
4 understanding as to the delivery of those payments into
5 trust at Sears for the Plaintiff's benefit.

6 As stated in the Eychaner case, the mere agency
7 relationship, that is, one where the agent in some way
8 manages the affairs of another, does not give rise to the
9 express trust. Id. at 134 through 35. Moreover, and I
10 believe dispositive here, the funds at issue were not
11 directed to be turned over immediately to the
12 seller/putative beneficiaries, rather, the agreement
13 contemplated that the funds good be held by contract at
14 least for 15 days and there is no prohibition on comingling
15 the funds.

16 Under those circumstances, the courts have widely
17 held that the parties have not established a trust
18 relationship, an express trust relationship, but, rather,
19 have established a debtor-creditor relationship. I would
20 note that there is not even an allegation that the funds
21 could be traced in the complaint, nor is there any
22 allegation in the complaint or any provision in the parties'
23 agreement that gives the Sellers any control over such funds
24 or requires them to be dealt with in a specific way to
25 enable their segregation or tracing.

1 The courts in this circuit, as well as in the
2 Seventh Circuit interpreting Illinois law, have concluded
3 under those circumstances an express trust, which requires
4 an ascertainable res does not exist. See LFD Operating Inc.
5 v. Ames Department Stores, Inc., In re Ames Department
6 Stores, Inc. 144 Fed.Appx. 900, 901-902, (2d Cir. 2005).
7 It's also worth citing the lower court, district court,
8 opinion on that issue, which appears at 2004 U.S. District
9 LEXIS 17575 at pages 12 and 14-15, particularly 14-15 as to
10 express trust. See also Chicago Cutter v. Carter-Karcher,
11 Inc., v. Maley, (In re Lord's Inc.), 356 F.2d 456, 458, (7th
12 Cir. 1965), Cert denied, 385 U.S. 847 (1966).

13 To be contrasted with those cases and
14 distinguished by the bankruptcy opinion in the Ames case is
15 In re Greenfield Direct Response, 171 B.R. 848, 857-858,
16 (Bankr. N.D. Ill. 1994) where the Court stated that there
17 was an immediate obligation to pay and, therefore, any
18 comingling was in violation of the parties' expressed
19 agreement. See also United States v. Mazza-Alaluf, 2011
20 U.S. District LEXIS 8391 at pages 14-17, (S.D.N.Y. Jan. 27,
21 2011) where the district court dismissed a complaint where
22 there was not only comingling, but no allegation, or any
23 plausible allegation. of any fiduciary relationship and,
24 therefore, the cause of action could not lie, even though
25 one could conceivably engage in various tracing mechanisms

1 because there was no plausible allegation of any fiduciary
2 relationship.

3 For those reasons the cause of action should, in
4 fact, be dismissed. It is alleged that I should take a
5 closer look at this matter because there are no cases
6 directly on point for e-commerce marketers like this. It
7 appears to me, however, that the general rules can be
8 applied to this relationship and, indeed, certain of the
9 cases bear a distinct similarity, including the Ames case,
10 to this case with one distinction, which is not really a
11 distinction that favors the Plaintiffs.

12 In Ames there was a similar relationship except
13 that -- and the same with Cutter/Karcher -- the goods were
14 actually physically in the Defendant's store. Here, of
15 course, they were not in the store but merely sold over the
16 Defendant's website. If there is a distinction there, it is
17 one that I believe is not meaningful, in any event, not
18 favorable to the Plaintiffs.

19 I will also note that in both Ames and Lord's, the
20 Chicago Cutter/Karcher case, the parties' agreement actually
21 had trust language in it. But both courts went behind the
22 language to determine that, in fact, there was no express
23 trust relationship in fact, given the permission to
24 comingle.

25 If anything by analogy here, and if one were to be

1 creating any sort of new law, I believe one would be guided
2 by the law of consignments and/or bailments, neither of
3 which is favorable here to the Plaintiffs under the Illinois
4 version of the UCC to affect an interest in consigned goods.
5 And, of course, there's no allegation of consignment here
6 but the facts might suggest a consignment type of
7 relationship that is effective as against prior creditors
8 and/or judgment creditors.

9 The consignor needs to perfect its interest by
10 filing a financing statement, Illinois UCC9-319, and the
11 official commentary thereto. That section deems the
12 consignee, i.e., Sears, if this were to be viewed as a
13 consignment, as having the ownership interest and,
14 therefore, the rights pass to the Trustee as property of the
15 estate under 11 USC Section 541. See *Leibzeit v. FVTS*
16 *Acquisition Company (In re Wolverine Fire Apparatus*
17 *Company)*, 465 B.R. 808, 820 B.R. (ED Wisc. 2012)
18 interpreting the Wisconsin UCC, which is on all fours with
19 the Illinois UCC on this provision.

20 As far as a bailment is concerned, "In Illinois, a
21 bailment is the delivery of property for some purpose upon a
22 contract, express or implied, that after the purpose has
23 been fulfilled, the property shall be redelivered to the
24 bailor or otherwise dealt with according to his directions
25 or kept until he reclaims it." *Maxwell v. Penn Media, (In re*

1 MarchFirst, Inc.) 2010, B.R. LEXIS 3480 at pages 19-20.
2 (Bankr. N.D. Ill., October 14, 2010).

3 Here the goods themselves could not conceivably be
4 part of a bailment because they are not delivered to Sears
5 to be held by Sears. Rather, they were delivered to the
6 customers. As far as the issue as to whether the money,
7 that is the proceeds, could be held as a bailment, again,
8 there's no language creating it and the limitations on
9 holding it are only contractual in the sense that payments
10 should be made, although not from this specific money,
11 within 15 days or when notified that a tax is due.

12 In addition, there is substantial doubt as to
13 whether there can be a bailment only on money. Id. at page
14 20 and footnote 6 therein, and see generally that if there
15 is a special deposit under Illinois banking law, there is a
16 bailment, such that instead of creating the relation of
17 debtor and creditor, the deposit creates a bailment in that
18 it sets apart the specific money for its return and demand.
19 Mid-City National Bank v. Mar Building Corp., 33 (Ill. App.
20 Ct.),1083, 1089-1090 (1975). However, a normal bank
21 deposit, where the funds go into the general funds is not a
22 bailment and the depositor simply becomes a general
23 creditor. It's an old case. Otis v. Gross 96 Ill. 612,
24 614, (1880) and In re Western Marine and Fire Insurance
25 Company, 38 Ill. 289 (1865).

1 Count 4 asserts that the Court should impose a
2 constructive trust on the Debtor's estate for the amounts
3 owed to the Plaintiffs. This is a bankruptcy case and the
4 courts around the country, including in the Second Circuit,
5 have clearly and uniformly stated that when a creditor
6 asserts or alleges as a remedy the imposition of a
7 constructive trust on a bankruptcy case, different equitable
8 considerations apply and that the Court should be very
9 careful, extremely careful to oppose such a trust or should
10 act with caution or that there needs to be a substantial
11 reason over and above normal constructive law to oppose
12 such a trust. See Ades & Berg Group Investors v. Breeden
13 (In re Ades & Berg Group investors), 550 F.3d 245 (2d Cir.
14 2004) and numerous other decisions in the Second Circuit,
15 including Rosen v. Chowaiki & Company Fine Art (In re
16 Chowaiki & Company Fine Art), 593 B.R. 699 (Bankr. S.D.N.Y.
17 2018) and the cases cited therein, where, as is aptly stated
18 by Judge Vyskocil, "Most significantly, even to the extent
19 that the debtor may have been enriched prior to bankruptcy,
20 the gravitational center of the equities analysis focuses on
21 the totality of the Debtor's creditors once bankruptcy was
22 initiated." Id. at 720.

23 As the Court there states, "No equities would be
24 served here by allowing Plaintiff to satisfy his losses
25 while similarly situated creditors, many of whom hold

1 similar causes of action against the Debtor for fraud and
2 fraudulent inducement, wait for pro rata distribution,"
3 citing Ades & Berg. Id. at 721.

4 Instead, as the debtors assert here, Judge
5 Vyskocil in the Chowaiki case noted that the Plaintiff may,
6 of course, file a claim, which is what the Plaintiff here
7 has done. See also Brenner v. Heller, 2011 U.S. Dist.
8 LEXIS 137072, (N.D.N.Y. Nov. 30, 2011), In re Paulino, 2014
9 B.R. LEXIS 4435, pages 20-21, (Bankr. S.D.N.Y. Oct. 20,
10 2014); and In re Fetman, 567 B.R. 702, 706 (Bankr. E.D.N.Y.
11 2017), and the cases cited therein, including Geltzer v.
12 Balgobin (In re Balgobin 490 B.R. 13), (Bankr. E.D.N.Y.
13 2013).

14 Here it has been argued that there are two grounds
15 for the imposition of the constructive trust. The first is
16 an alleged trust or fiduciary relationship. And the second
17 is wrongdoing in the form of alleged misrepresentations, all
18 of which occurred on or after the commencement of the
19 bankruptcy case. Besides, even if one were to conclude that
20 that grounds would give rise to a constructive trust, they
21 would only apply to the money advanced allegedly on the
22 basis of those representations, which is a small fraction of
23 the total amount at issue here.

24 Moreover, as to those representations, it is
25 alleged that such representations were made system-wide to

1 marketplace sellers across the board, which consistent with
2 the case law that I've just cited argues that if a post-
3 petition claim is to be based on such representations, it
4 should be pursued as part of the claim process for assertion
5 of a post-petition claim, which is already underway with
6 regard to these two Plaintiffs and should not be used
7 through the remedy of constructive trust for one claimant or
8 one alleged recipient of such misrepresentations to get a
9 leg up with a specific property interest over others.

10 Particularly, whereas here there are issues as to
11 tracing, assuming that tracing had been alleged in the
12 complaint, that could only be dealt with by tracing
13 mechanisms like the lowest intermediate balance rule, which,
14 when one takes into account other parties who necessarily
15 receive the same or similar representations, would be unfair
16 and inequitable.

17 Under Illinois law, constructive trust is imposed
18 to prevent unjust enrichment by imposing a duty on the
19 person receiving the benefit to convey the property back to
20 the person from whom it was received. *Martin v. Heinold*
21 *Commodities, Inc.*, 163 Ill. 2d. 33, 643 N.E. 2d 734, 745,
22 (Ill. 1994). It is a remedy, in essence, for restitution. A
23 property seeking a constructive trust must establish the
24 existence of identifiable property to serve as the res upon
25 which a trust can be imposed and possession of that res or

1 its product by the person who has to be charged as the
2 constructive Trustee. People es rel. Hartigan v. Candy
3 Club, 149 Ill. App.3d 498501 (N.E.2d, 1988, 1991, Ill. App.
4 Court 1986).

5 Here, as I said, there are two grounds. I will
6 return to the second ground, the alleged fraud, but as is
7 clear from my statement so far, I do not believe that under
8 the law governing the assertion of the constructive trust
9 remedy in a bankruptcy case the allegations regarding fraud
10 establish a basis for that remedy here, separate and apart
11 from whether a constructive trust would lie in any event,
12 which I'll come back to.

13 Let me go, instead, to the first basis for the
14 remedy of constructive trust, which is allegations that
15 there was a trust relationship between the parties, albeit
16 not a formal express trust relationship and/or that the
17 parties' relationship itself, separate and apart from the
18 alleged misrepresentations, created a basis for imposing the
19 remedy here.

20 We discussed at oral argument whether there are
21 sufficient allegations in the complaint of duress or
22 coercion. I conclude under Twombly and Iqbal there are not,
23 particularly given the allegations in the complaint and the
24 marketplace agreement, including the statements by the
25 parties that they're acting as independent contractors, and

1 the volume of business that the complaint alleges is done
2 here. Under those circumstances, the recitations of duress
3 and/or coercion are merely restatements of the cause of
4 action as opposed to the facts supporting the cause of
5 action and/or are not plausible.

6 The other basis for a constructive trust here is
7 that the parties were in a fiduciary relationship with
8 respect to some identifiable property or res that is one
9 where a proper remedy would be the imposition of a
10 constructive trust. Here again, the only possible res that
11 would be the subject of the trust would be the funds paid by
12 the customers into Sears, which, under the agreement, Sears
13 is to pay a like amount absent or after having deducted
14 commission and certain other amounts within 15 days to the
15 Sellers and/or after the Sellers notify them with taxes due.

16 The complaint itself does not set forth expressly
17 any facts which show that that relationship, which is,
18 again, laid out in the Sears Marketplace Agreement, would
19 give rise to the type of fiduciary duty that would justify
20 the imposition of a constructive trust even outside of a
21 bankruptcy case. As I noted, there is only one statement of
22 an agency relationship and that is only in respect of one
23 sentence in paragraph 1B. Quote, "Seller hereby appoints
24 Sears as an agent of Seller for the sole and express purpose
25 of receiving payments from users for Seller's merchandise

1 sold on the websites."

2 Illinois law recognizes the common law presumption
3 that a party in possession of personal property is, in fact,
4 the owner. The property here being the cash paid by the
5 customers. In re MarchFirst, Inc. 2010 B.R. LEXIS 3480 at
6 page 16 and the cases cited therein. That presumption
7 extends to money. Id. That presumption can be overcome and
8 it can be done by showing a proper agency relationship as
9 applied to the particular property. That is because in
10 Illinois, "Agents generally do not own property transferred
11 into their possession by or for the benefit of a principal."
12 Greenfield Direct Response, Inc., v. ADCO List Management
13 (In re Greenfield Direct Response, Inc.) 171 B.R. 848, 857
14 (Bankr. N.D. Ill. 1994).

15 On the other hand, the burden of establishing an
16 agency relationship rests with the party claiming it, in
17 this case the Seller/Plaintiffs and "In Illinois, parties
18 have an agency relationship when the principal has the right
19 to control the manner in which the agent performs his work
20 and the agent has the ability to subject the principal to
21 principal liability." In re MarchFirst, Inc., 2010 B.R.
22 LEXIS 3480 at pages 17-18 and the cases cited therein.

23 Here, as we discussed at oral argument and as is
24 clear from the Sears Marketplace agreement, even though
25 Sears is stated as the agent for receiving the payments,

1 there is no control over that property by the
2 Seller/Plaintiffs. Indeed, it can be comingled, consistent
3 with the case law that I've already cited. Therefore, it is
4 clear for purposes of a motion to dismiss that such property
5 is property of the Debtor's estate and should not be
6 impressed with a constructive trust given that, although
7 Sears is stated to be an agent for receiving the property,
8 it is not a true agent there for fiduciary duty purposes.

9 In that the Trustee or putative Trustee does not
10 have a sole duty to deliver title and possession of that
11 property, i.e., the payments by the customers, back to the
12 Seller/Plaintiffs. Id. See also Brandt v. ICON EAR, LLC
13 (In re Equipment Acquisition Res., Inc.) 2012 B.R LEXIS 4651
14 at pages 11-12, (Bankr. N.D. Ill. Sept. 30, 2012). See
15 also Sullivan v. Glenn, (In re Glenn) 502 B.R. 516, 452-543
16 (Bankr. N.D.Ill.2013) discussing, consistent with the
17 parties' own representations and agreement in paragraph G,
18 the Illinois law under which one would be deemed an
19 independent contractor instead of an agent with fiduciary
20 duties.

21 It's clear to me under the allegations in the
22 complaint and the Sears Marketplace agreement that there is
23 no such duty here that would give rise to a constructive
24 trust for failure to comply with the duty, even outside of
25 the bankruptcy context. Although, again, the allegations

1 here are so similar to what is described to me by the
2 Plaintiffs as a system-wide allegation that the bankruptcy
3 context would argue strongly for not imposing a constructive
4 trust even if such an agency relationship were sufficiently
5 pled in the complaint, including as I must take into account
6 the parties' agreements, which is incorporated into the
7 complaint.

8 It also appears to me that as a matter of
9 constructive trust law outside of bankruptcy, the alleged
10 what I'll call misrepresentations by the Debtors, which are,
11 in fact, quoted with the emails having been attached as an
12 exhibit, are of such a precatory or couched in future terms
13 nature as not to give rise to a fraud. But that conclusion
14 is not necessary given the fact that those post-petition
15 allegations, or allegations of post-petition misconduct, are
16 quite properly or appropriately encompassed by the
17 litigation of the Plaintiff's post-petition administrative
18 expense claim, which are being dealt with under the opt-in
19 procedures previously approved by the Court.

20 It appears clear to me, therefore, that there I no
21 independent duty arising prepetition that would give rise to
22 a constructive trust remedy and then all that is covered by
23 these allegations is the failure to pay a debt. Failure to
24 pay a debt is, obviously for anyone who has been in that
25 position, extremely irritating and worse condition to be

1 under as the creditor, but it does not create special
2 interests in property. Rather, it is dealt with in the
3 claims process as opposed to a trust or constructive trust
4 process. See Swanson v. Randall, 195 N.E.2d 656, 660 (Ill.
5 1964)

6 As far as the last cause of action is concerned
7 for conversion, as I've already found, there is no specific
8 property right or interest here in the funds held by the
9 Debtor, which not only are comingled but were permitted to
10 be comingled by the parties' agreement and the operation of
11 law. Given that conclusion that I've already reached based
12 on my review of the complaint and the parties' agreement, a
13 claim for conversion does not lie. There was not right to
14 the specific funds paid in by the customers but, rather, a
15 claim for payment of a like amount within 15 days or upon
16 notice that taxes were due.

17 Under those circumstances, a cause of action for
18 conversion would not lie. There is no separate tort other
19 than, that is, the breach of that obligation to pay a like
20 amount of funds over or within 15 days. To the extent it is
21 a separate defense, other than just simply the fact that
22 there's no property interest here to be protected, the
23 Debtors correctly cite to the economic loss doctrine as
24 recognized in Illinois, where if there is no separate tort,
25 and there cannot be a separate tort here given my conclusion

1 based on the allegations of the complaint, if there is no
2 property interest in the funds that have not been paid and
3 one, therefore, is looking only at a breach of contract, a
4 claim for conversion would not lie. See *Congregation of*
5 *Passion v. Touche Rosse & Co.*, 636 N.E.2d 503, 514 (Ill.
6 1994) and *Essex Insurance Company v. Lutz*, 2007 WL 844914 at
7 page 5, (S.D. Ill. March 20, 2007).

8 So, I will enter an order granting the motion to
9 dismiss each of the remaining causes of action in the
10 complaint. That order, just for good housekeeping, should
11 also confirm that the other causes of action have also been
12 dismissed and/or withdrawn based on the Court's ruling from
13 March 13th that under Bankruptcy Rule 7001, such causes of
14 action should not be brought under complaint but, rather,
15 should be consolidated with the pending administrative
16 expense matters and/or with regard to prepetition claims,
17 the general claim disallowance process or claim objection
18 process under Rule 3007 of the Bankruptcy Code, in each
19 case, for consolidation purposes under Bankruptcy Rule 7042.

20 So, does anyone have any questions on that?

21 MS. CROZIER: This is Jennifer Crozier for the
22 Debtors. No, and thank you. We will submit the order.

23 THE COURT: Okay. All right, thank you. And that
24 order does not have to be formally settled on notice to Ms.
25 Kramer, but you should not only copy her on the email of the

1 chambers but also give her a day or so to look it over to
2 make sure it's consistent with my ruling.

3 MS. CROZIER: We will do that, Your Honor.

4 MS. KRAMER: Thank you, Your Honor.

5 THE COURT: Okay, thank you.

6 MS. CROZIER: Thank you, Your Honor. I think that
7 completes our agenda and we're on, I believe, for April 23rd
8 for our next omnibus, right?

9 THE COURT: Okay. Very well. I will be talking
10 to you all then. Thank you.

11 MS. CROZIER: Thank you. Be well, everybody.

12 THE COURT: Same to you.

13 (Whereupon these proceedings were concluded at
14 12:02 PM)

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C E R T I F I C A T I O N

I, Sonya Ledanski Hyde, certified that the foregoing
transcript is a true and accurate record of the proceedings.



Sonya Ledanski Hyde

Veritext Legal Solutions

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Date: March 26, 2020

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